POLICE & FIRE PENSION ADVISORY COMMITTEE
FEBRUARY ?, 2003

Members present: Jim George, Michael Donnelly, Mark Westphalen

Members absent: Mark Meyerson, Joe Yindrick, Aaron Drake

Personnel Dept.
Resource Staff: John Cripe, Paul Lutomski

JG: I guess I will act as Chair then. Officially start the meeting. If that's okay with everybody. I immediately move that all meetings be suspended where the outside temperature is – *(Laughter)* not above freezing.

??: I would vote for that.

PL: That's two. *(Laughter)*

??: That's it.

??: We're done then.

JG: Oh-kay. Do – Does anybody make the motion that we approve the minutes of the last meeting?

??: So moved.

JG: Second?

??: Second.

JG: All in favor?

(Present committee members say, "Aye")

JG: Motion is approved. Then I'll turn it over to Paul.

PL: Second item is that on December 1st of 2002 we invested a million dollars as planned in the Smith Hayes Capital Employees Limited Partnership, and we then abruptly lost .02% of that million dollars and we're at $998,800 at the end of December 31st. They haven't calculated the January rate. In fact, we just got this 998 figure on January 16th. They send the figures out every quarter to be calculated. They calculate these return figures on a quarterly basis, and then they send them out to an independent auditor for calculation. So we're going to have to wait. We won't be able to use the figures right away. We'll have to just use the most recent valuation we have when we calculate employee market values. The next thing to happen was on December 20th we received our actuarial reports. We gave copies to the Council and a little bit later then mailed copies to all the advisory members and copies to the Mayor's Office. The big news is that our funding level decreased from 104.4% to 98%. That – Basically that wasn't any surprise. To people on this committee anyway. The decrease in that funding level was due to the City contributing less than we had been requesting for the last several years, and because our asset return rate was less than the assumed 7½% for at least the past few years. Market value, however, for that fiscal year was 3.37. The fiscal year ended August 31st. And then something completely different is what they use – a rate of return on the funding value of 4.11. We've spoken about that before, but what they do is they take a four year smoothing method, so that in years where we are losing money or not earning the – yes, have a negative return or under the seven and a half, that is kind of softened the corresponding earned above the actuarially assumed rate. We don't get the full benefit of that immediately either. That will be softened on the way up. Hopefully, we will be going up someday. Then we calculated the return rate for the calendar year and that was 3.2995, which doesn't sound like very much, but compared to the average of negative 8.6, for the average U.S. pension plan, 3.2 sounds pretty good. It's about ... what? 12% above the average. Then, also, on page 52 of Pensions and Investments magazine there's a – They list the top, I think two hundred, or three hundred pension plans in terms of size. Nebraska Investment Council, their assets decreased 6% from a year earlier from assets on the 30th. Of course, the 6% is after the employee and the employer's contributions are put into it. This just measures how at that market value on September 30th. So that tells you that their return was probably closer to a negative fifteen. I'm just guessing, on the percentages. So 3.2995 we're fairly happy with that.

??: Very good job.

PL: On January 1, then, as scheduled, we invested a million dollars in the J.P. Morgan Multi-strategy Fund, and those January rates are not calculated. They sent me the December rates. Of course, we didn't have any money with them at that time, but it earned 1.86% through December. On January 14th, I'm sorry I misspelled Michael. The "a" and the "e" are switched around, but the City Council unanimously approved. Which I don't know if unanimous is a word that they are – used with the City Council.

(Laughter)

??: You've got that right.

PL: But they seemed to like Michael Donnelly, so ....

??: Historic event.

MD: I'm wondering if it's me or some other Michael.

(Laughter)

PL: On the 16th then, we sent the budget request asking for 3.3 million dollars. That is for normal cost plus a dollar amount necessary to eliminate something called NPO, or Net Pension Obligation. Before we get into what that is .... So, 3.3 million is our budget request for fiscal year 2003-2004. Then after that, it goes back down to 3.1 because we're pretending that they're going to give us the 3.3, and that we earn 7½%. Back up to 3.3, which is full normal cost again. 3.4 and 3.6 which are full normal costs based upon 4½% wage increase and 7½% interest rate assumption. But every year – Well, we ask for – we send in a budget request and it's a five year request. So it gives them a heads up, as to how things are changing in the future. We are currently getting 1.6 million dollars, almost 1.7 million dollars, and when Georgia and I talked to the Mayor earlier about the budget situation as regards to the pension, he said he'd be willing to try to get a half a million dollar increase for this coming budget year, rather than the standard $250,000 increase.

??: Was this before or after you budgeted the 3.3 million?

PL: That was before. I told him about the 3.3 million, so he knew that, but he didn't think that there was any way we could double what they were contributing. So, go from $250 to $500,000. Of course, he won't be Mayor, anyway, when the budget is passed, so we'll have to approach the new person, and see what they say.

JG: Is it just me or does that strike me as, as bad management?

??: Poor management.

??: By the way, when you're pension actuarial costs are 3.3 million dollars and it would appear to me the Pension is making the recommendation, and that's what they're paid to do, on what those contributions are supposed to be at or set, and they're saying the City should contribute 3.3 million dollars, but yet the City doesn't want to do it. Because money's tight. I mean, money's always going to be tight.

JC: Well, it's pretty tough, because it's – It's kind of rhetorical for us to answer the question, because if he – if you look at the request we made, like six years ago, or seven years ago, if they had followed the request that we were making at that time, you wouldn't be looking at a large increase. The incremental increases we were asking for would have eaten up the additional amount and we would be near normal costs. There would be an increase, because we – the earnings have dropped off the last two or three years, so we would have earned less than assumption, but the requests we were making to catch up on normal costs would have been there, so. We made the point, and we tried to make the point with this administration, and budget before that, that you have to kind of get to where you need to be in order to not fall that far behind, and they were willing to let it drift. And we drifted off. It's easier to make incremental increases than it is to fall behind and make huge increases, and that's where we're going to be. And if they don't do it this year, then we'll be even further behind.

??: That's my point.

JC: And it gets more and more complicated and a lot harder to get the right answer. So it becomes a larger burden . When this Mayor came in office, we met on budgeting the very first May. It was like May 30th or whatever. At the very first briefing, I said, “Before your term’s out, or the first part of the next term, we’ll be underfunded, unless we make corrective action.” That was the very first week or two, and here we are four years later and it looks exactly like we thought it would. Some of it has to do that the market wasn’t quite as kind as it needed to be in some areas, although we worked as hard as we could to earn a positive amount. It wasn’t good enough to get us that 7½, but – So, it’s a rhetorical kind of question. I mean if we – No, it’s going to be extremely hard for any Mayor coming in to address the needs where it is today. Because something will have to lose. Somebody has to lose now. Some department has to lose, or lots of departments have to lose, or we have to be honest with the public and raise taxes, and that’s hard for politicians to do. It wasn’t quite as hard when we were asking for $200,000 a year incremental increases. It’s harder now.

PL: To kind of segue into the next thing. Net pension obligation. Since we are now less than 100%, the City’s external auditors have asked us to calculate what they called NPO, by using the governmental accounting standards for statement 27. That was where they outline how NPO needs to be calculated. So I worked with the Finance Department, the external auditors and we pounded this thing out , but what it shows is that for fiscal year 2001-2002, which is the reporting period on this next City’s annual consolidated annual financial report, which is a big book that the City puts out on their financial statement that all of bond rating agencies look at. For this next reporting period, the City will have a negative NPO, which is a good thing. A negative obligation. So that means according to these accounting standards the City has been putting in actually a little bit more than what the accounting standards required them to be putting in. To the tune of $374,000. However, while that was for last August 31st of 2002, we’re already more than halfway into this next fiscal year. Assuming 7½% return, the projected NPO, because we basically know what the City’s going to contribute for this fiscal year, the 1.6 million. We’re going to have a positive $247,000 NPO, which is a bad thing. It means we have an obligation, and they’re going to have to show – I talked to the Finance Director – that if they’re going to have to show this $247,000 as an obligation that the City has to the pensioners. So it’s like a liability. The City owes us $247,000 based upon this accounting procedure. Then if you add in the $500,000 that I don’t know if we’re going to get, the increase, on top of our 1.6 million, add another $500,000, the projection for 2003-2004 is a positive NPO one million two, still. Which is a bigger number, so that’s worse yet.

JG: Well, wouldn’t the number be even bigger if the actuarial normal cost is 3.3 million and we end up putting in 2.1 million?

PL: Well, this is based upon the 2.1 million.

JG: That’s the difference between 2.1 and 3.3?

PL: No. Well, the accounting rules do a kind of a smoothing thing. But this is based upon the City putting in 2.1 million dollars instead of 1.6. Because he said, “I’ll try to give you an extra $500,000.” So I went from 1.6 to 2.1, and that’s what this is based upon. This assumes 7½% income.

JC: And we got some credit four or five years ago, where there was a period in one of the actuary's reports, and I don't remember which year, where the actuary said, "On a short term basis, you don't need to make any contribution." And the City made a contribution. I mean, they were making contributions anyway. But a small one anyway. Well, and that carries forward as a plus. It doesn't seem like much, but it's a plus. We were still knowing mathematically that we were not going to be able to come out ahead long term. But on a short term basis, one year window, we didn't have to make a contribution and the City did. But, Paul, I know that's the same year we were making a request saying, "You need to put more in." But the mathematical calculation based on how the auditors do it got you a plus. Got you a credit. And it carries forward. So they're working on a little bit of credit for this year.

JG: What about all those years they didn't put in what the actuary recommended?

JC: Well, we were plus. We were still plus overfunded. And that overfunding actually funds the pension.

??: Through your earnings.

JC: Right. So the City isn't in –

JG: Now we're not overfunded.

JC: That's exactly correct. So this is the first time and, of course, the accounting standards have changed, so for the first time –

PL: That's the calculation right there.

JC: Right. So for the first time, life has changed for Finance and for folks.

PL: This only has to start since 1996. I think that's the year ....

JC: So this is the first time that life has really changed for these people, because we have not been in this position with these accounting standards and with a deficit, so to speak, with regard to 100% funding. So this is the first time it will be kind of a public issue. We tried to bring this up last during the Task Force. You all remember when we –

??: Oh, yeah.

JC: And W. Don says, "Oh, it's not a big deal. Nobody cares." Well, yes, it is a big deal, and it is a bigger deal than folks were giving it credit. Underfunding in today's defined benefits is not good. It's not good for us and it's not good for the City.

JG: I guess my point bringing this up is, is now the time we could use it to our advantage? Money is always going to be tight, it's always going to be hard to get an extra 500,000. I mean we could be 80% funded, and the City could still come back and say, "Now we're going to get you another

$500,000." We could do this all the way down to zero.

PL: Well, I mean we did use this, when we spoke to the Mayor about going from 250,000 to 500,000. I think John will have to talk to the new Mayor.

JC: That was the only meeting I ever had with this Mayor.

??: Four years ago?

??: That was your one shot.

JC: Yes. Paul and Georgia have had meetings with the Mayor. I have not.

PL: I've met with him twice.

JC: I've not been invited.

PL: I met with him actually, yes, twice. That's it.

??: Two times. Well, never mind.

JC: I'm a Democrat, by the way.

??: Oh. I'm a Republican.

JC: I don't think he thinks so, but so. No, but that's the problem. I don't know if you really wanted to know the answer. And I'm a little bit more forceful, obviously, than Georgia and Paul. And I'm not afraid of my job. And Georgia's appointed. I mean a little quick honesty while we still have the tape going. We'll cut this out a little bit out of the minutes.

??: It's a surprise to me.

(Laughter)

??: That's fine.

JC: As you know, I'm just being pretty straightforward. I've not met with him about the pension, since that day.

??: I know. I know.

JC: And I told him that, you know, in this four year period, you're going to be faced with huge issues.

PL: And it wasn't that you refused offers to meet with him.

JC: Oh, no.

??: Oh, I bet not.

JG: But on the other hand, even when you did meet with past mayors, the results were the same.

JC: Well, we got the, we got Johanns to guarantee to at least a standard amount, you know, there was a period where he was – we were at 200 or 150,000. I think it went to 450 and we did 450 for three years. That the result of us direct discussions about you've got to do a better job, you've got to be more straightforward and we increased from 150 or 200 to 450 and we did that for three years. Yes, yes, it makes a difference. Because this is huge. And we never talked to the Council. We were not permitted to talk to the Council ever about these issues, despite the little task force song and dance last summer. So I think whoever becomes Mayor has a huge hurdle to overcome, and part of it is that you're now in competition with one another. Every department now wants this money. And if it's dealt with as a timely basis as a real manager, you don't have to be in competition with one another.

JG: Who has the fiducial responsibilities of funding the pension? Obviously we're *(sound of cough)* at this point, unless we get a board of trustees. It's not us. Is it you? Is it Georgia? Is it the Mayor? Is it all of you?

JC: Well, actually it's pretty. I mean, we've fulfilled our obligation by notifying them on a regular in writing every time, every spring that they're not living up to their contributions, or we give them notice that they're not doing their job. So we've been telling the mayors and Finance and Budgeting that they're not pulling their weight.

??: And I believe that.

JC: And we've kept them, by the way. So the fiduciary responsibility really is in the taxing authority, and that's the City Council responsible. And their ultimate responsibility is with the City Council and the Mayor. As a group. Now, they – You all know that they only get what people tell them.

JG: The Council never hears this.

??: Well, the Mayor does.

??: But they have in the past. I mean, this year I think you guys did a good job of bringing it up to their attention.

JC: I met – We met privately with three Council members. The Republicans, who would meet with us. The Democrats did not. By the way.

??: They would not meet with you?

JC: We asked them.

??: Or they chose not to.

JC: They chose not to. We invited them right after the election two years ago. And we met with, and the three. You can't have a majority, by the way, or it would turn it into a meeting. So we asked them to if they would like to meet individually, and the three Republicans did meet with us and we were pretty straightforward about it. And they've been pretty positive. You could see in each of the last two budget meetings, those folks have been talking about adding money, and not getting the support from the other folks. So once we had a chance to tell them about the condition and talk to them seriously about it, they've been more positive about adding funds. So. But I don't have great hope that this will be resolved. But I would think that a new Mayor was going to have to take a bigger chunk out of it than we've had in the last couple years. So I'm hoping that after we get a new budget in place that we'll be not adding 500, but three quarters of a million or a million, because you have to take bigger chunks now than you would have before. This is a pretty big egg to drop on whoever gets elected. Because you really have –

??: I think maybe it behooves us – I don't know when you guys think – timing is the right time to start talking to the City Council again about this, but I think, if you think now is the right time, that's fine.

JG: If we don't do it now –

??: If you think a couple of months from now, or –

JC: Well, I think –

??: We just need to have another series of discussions with them, to talk about the impact.

JC: I do think at some point it's important to ask the, if it becomes two candidates and you won't know until after people can register, you know, after, what is it? March 6th. So if you have two candidates for Mayor, I think it's important then to ask them if they would like a complete briefing on the pension. So at that point, perhaps, a couple members from your committee and a couple members from our staff, Paul and I or Georgia, a couple members from the committee, set down with them and get a complete, full and complete briefing on the pension. I think that's appropriate. Then they're prepared to understand what a big hurdle they have. Not to blame another administration, or not to blame any body else, but I think they have to understand what they are inheriting, so that they're prepared to move forward. If there's a suggestion, that's where I would suggest we move. Now, they're both Council people, so they more than likely will be irritated that they haven't had a chance to, you know, take a more active role. You know all of this would have happened on Coleen's watch. Not so much on Glenn's, but he's only been here two years, or he might have been in the same boat. But I think once you get to that point, perhaps, we should do that as a Committee, and if you want to make a motion or something that we involve the Chairman of the committee or a representative of the committee, and the civilian members or something and a couple staff members to contact. Now if there's more than two candidates, we – You couldn't do it until after the primary. Until you actually got down to the two candidates, each of which may be your mayor. Because the budget will be in preparation.

PL: I mean we know that Glenn Friendt will still be a Councilman. Jon Camp will still be a Councilman.

JC: Well, but see you're talking about –

PL: The only one you don't know about is Svoboda and *(indecipherable)*

JC: I think the emphasis actually – The budget is prepared for them. It's the – It's the Mayor's budget.

??: Prior administration.

JC: It's the Mayor's budget.

??: Right.

JC: And it's being prepared today. By this Mayor. To be submitted in the first week of June. So when you're talking about preparation, you need to have the two candidates that survive the primary, so that they know that when they get into office May 20th, they've got two weeks or three weeks to modify the Mayor's budget, and to do whatever they need to do, and this is a critical piece of that review. So somewhere between April 6th and May 6th or May 8th, whenever the election is, you should ask for an opportunity to brief them. Both of them at the same time at the same location.

??: And prior to that, take the opportunity to revisit with the City Council one on one, or –

JC: Well, however it will turn, because there will be some people who will not make the election and there will be some people that will turn over, and you may want to do that in June. Because the Mayor's, any –

??: Use the top down approach.

JC: Right. Any modification that happens to the budget gets modified after it gets presented to the Mayor, by the Mayor. So, in order to get the appropriate dollars in the budget to begin with, it has to be in this two week window. Any modification and you really have a pretty tight time window there.

??: Okay. Whatever you think is best. Because you guys would know more about that.

JC: I'm not all that great on politics, you can tell. But I would think that you –

??: But you know the timing. If you think that's the proper timing, then that's fine.

JC: I would think that we make an offer anyway. If the two turn us down, then they just turn us down. But, you know, I would think our staff plus a member of this committee and maybe one of the two you. So you guys can report back at our May meeting about the briefing, because it will be the week before the election. Now, we're not looking for a commitment, we just want them to know what the circumstances are of what the pension is like and how it got to where it is and they can ask whatever questions. But they are in competition. Every department will be in competition with one another for the same million and a half dollars that we'd be asking for, and it will be a huge deal. So if that sounds appropriate, we could go forward. I guess we don't really need a motion, but we could contact the Chair of the committee and one of you two gentlemen if you're interested.

??: I would think a motion would be appropriate though.

JC: If you want to authorize it, we'd certainly try to move forward. Now, if they decline our invitation, then, you know, we're stuck. But if you're talking about funding that's the appropriate time.

JG: Do I hear a motion then about that?

??: Yes, I'll make a motion that we meet with the two potential candidates and .... you can fill out the rest of it. (warn them of the impact of current underfunding of the Police & Fire Pension and what we see as the solution.)

??: Second.

JG: Motion made and seconded. All in favor, say "aye".

(Present committee members say, "Aye")

JG: Opposed?

(Silence)

JC: We'll clean up the motion.

PL: Okay we have a couple more things. We just already talked about sending out the letters to active retired DROP members. I have copies to Mr. Donnelly and Westphalen. Finally, on the recent events, we hired the same computer programmer that looked at our pension analysis estimate system. I hired her back on February 3rd to have a look at as much as possible of the rest of our system. I have given her a document and she's been looking at things and she's pretty darn sure that she can't look at everything in a month, so I've been prioritizing that, and what I told her to concentrate on is just the majorly(?) (major league?) critical things. Basically the inputs into pension analysis. Are we calculating base salary correctly? Are we pulling the right earnings codes off of Tesseract system, adding up fake salary, applying the correct deduction rate. 8%, 7.6%, 7.0%. To take our contributions. So that's her first priority. After she does that, *(indecipherable)*.

JC: We don't have any feeling that they're wrong. We just think it's a good opportunity to – she was available, we think it's a good opportunity to use her skill to review where we stand.

PL: Rather than start with a whole brand new person that doesn't know anything about our system.

They called us at the end of January and said, "Call us, and it will be done, available February 28 or so.

JC: She did a good job on redoing the other pieces. Streamlined the language.

PL: And then I mailed out an asset investment plan. Larry and Lee at that time anyway recommended investing $5 million into the Calvert Social Index Fund as per run by the Vanguard Corporation. There's a Calvert Social Index that has large expense fees and then Vanguard mimics that fund for 25 *(indecipherable)* points. After talking to Mr. Donnelly a little bit about this, I think he has a good point and John also made several points, as to why we could wait and have a closer look at this. A more global restructuring might be appropriate. So we were thinking that instead of immediately dropping $5 million into this fund, we would contact Smith Hayes and either they could do an analysis themselves or they could hire someone to do an analysis for them, but it wouldn't cost us anything, wherein they would say, "Of your equities, here's how we think they should be invested." What we're looking for is kind of a two-tiered thing. First off, what we have here: Domestic, Europe or Asia, Management style should be active or passive, value or growth, the percentages and capitalization, and if you folks have any other recommendations. But we want to nail down those large characteristics first before we choose the specific investments that we're going to use to accomplish that. It's got to be what their, or who asked them to do.

JC: Paul and I have been talking in the last three or four months as we put this together. There's so much instability with regard to what we are doing with Iraq and there has been so much fluctuation. If we really wait to address this in May, we're not going to be any worse off than we were, you know, today. If we have an invasion, it's more likely going to be in March or early April. If we meet again in May. I mean we've got some time to revisit this. We were thinking that in the early part of December when we were talking about the asset mixture, things were looking fairly good for early January as starting to turn around. Things have kind of soured a little bit and maybe we should just take our time a little bit. Hold that money in cash. Get a little bit more time to review. I don't see any negative to waiting, so unless somebody has an objection, we could – we will hold off until May.

PL: Even if we wait, we'll still have almost $40 million in *(indecipherable)*. So if there is a war, and the market bounces, in an upwards, we're not going to miss out on that. We're just going to be missing out on $5 million worth of that.

JC: Right. We still are proceeding with the other investments, the strategic investments we're making with so much a month and so much a quarter, and all those kinds of things we were doing before.

PL: We're putting $300,000 a week into the Calvert Bond Fund. We're putting another million dollars on April 1st into J.P. Morgan, and then two more quarters after that. So we're going to continue with all of that. Maybe it's better to have them closer, the closer with our equities, and get some more mid-cap and some more small cap.

JC: Well, we have one more strip left that we have hanging and we will be selling sometime this spring. And we're looking at the right time to sell it, and it fluctuates so much. You know you think it's getting close to the right time to sell and then it bounces down and up and down and up. So. Unless somebody has some huge objection we'll can just wait until May and then revisit the analysis.

MD: No. I think it's a good idea. Part of my conversation with Paul earlier today was how can we round out our equity positions, to perhaps diversify a little bit more to help reduce the risk and at the same time, and that's what the whole investment plan is looking at. Perhaps enhance our total return and diversification is, of course, one of the best ways to do that. We talked about how we were going to increase our funding, or build up more assets. This is one of the ways we can do it, perhaps.

MW: I found it interesting. I met with – We had the opportunity to meet with the market, the chief market strategist for Van Campen Mutual Funds here a couple weeks back. This guy comes out and he talks about his style allocation, which I knew we were going to be talking about that today, and he says, and this is dated January 13th, 2002, he believes the allocation should be 65% stocks, 25% bonds, 10% cash. Within that stock allocation, 30% large cap growth, 20% large cap value, 35% small cap growth, 15% small cap value. Within the fixed income piece, he believes it should be 50% high grade corporates, 25% high yield munis, and the remainder in Caldwell Federal Agencies.

(Whistle)

PL: Well, this is good. I mean that's the kind of stuff we're looking for, right there.

MW: Yes. I mean I have never seen that kind of detail on what your allocation assets.

JC: This is what you ought to buy right here. This is it. What to follow my stuff, buy this.

PL: Can I have a copy?

MW: Yes. You can have that.

JC: Well, it's kind of fun for us when we – American Funds and Smith Hayes funds are just – Paul and I to go to American Funds headquarters to talk to their economist in Los Angeles shortly after 9/11 and we flew out, and we had lunch with one of their chief economists and he was talking to us about where he thinks the future is going to go and we're just having sandwiches and I thought these guys were going to get sick, because he was telling us corporate bonds are the way to go. They don't sell corporate bonds. And he says, "the spread corporate bonds, if I was going to buy investments, that's where I would put my money." That's an honest return. That's the way people ought to do business. Because he was telling us, "Look, you want to make some money in the next year or two years, the spread between corporates is where you ought to have some investment, and we didn't have exposure, came back and bought the Calvert Fund, we did some research and thought he was right and bought into the Calvert Fund, think it's a good solid fund. Prior to that, everybody's going, "You've got to put here, you've got to put here." He's telling us about products that they don't even sell. That's solid advice. I mean that's – He's looking at the real market and says, "This is where the weakness is, and this is where you can make some money." And those kinds of things are almost invaluable. Because those are things you don't pick up by just listening or reading in a passage some place. But this guy has good detail. The guy that we met with told us some stuff that I think these sales people are going to just pass out, because they wanted to sell us something else. But you know that's where you actually find out whether people are being tremendously honest with you. What are you selling and what do you want us to buy? And they recommend something entirely different. And I was surprised. But it was good advice for us and it's been good. It's a good place for us to put our money.

MD: Well, it's amazing when you talk to strategists and some of the lower level economists, they will not get to the point where they're talking specifically about the products for that company. And I know Dr. Soll is very similar to Wells Fargo. You know very seldom does he get down and say, "Buy Wells Fargo." He'll do just like the VanCampen strategist said. He'll say, "These are the areas that I think look attractive now. Based on this asset allocation model, this is what I would go after now." You find the consultant or investment adviser to help you with the individual stocks, bonds and funds.

JC: Yes, and the guy from J.P. Morgan was the same way. When we had lunch with J.P. Morgan's guy, he was telling us about where he thought the economy was going to go, and how life was going to be, and there wasn't a single item on there that says, "This is J.P.'s funds, you ought to have a $10 million in this, because this is very good." His point was this is the way the world looks and these are the possibilities in this market for making some money and this is the possibilities for not making money. I think that's good advice, and we like to listen to all those kind of things.

??: Well, I mean the theory and the philosophy that I think we have in this Board is different. When salespeople sit across the table, I mean the thing that comes across the mind, I hate to say it, is what can I position that they will buy? Because what they really need and what they will put cash down for are two different things. And right now in this market people are not necessarily making the right decisions. They're doing what they think they ought to do, which is really bass-ackwards from where they need to be. I think we're on the other side of that time frame or I believe we are. Where we're looking at the things what should we be doing now to maximize the returns that we need down the road, and we're not necessarily fearful of the marketing media thing. And I think that's where we need to be. That's where talking to these people are very helpful, because they will tell you what you really need to hear and know, because they don't have anything to hawk. When they're talking to you.

JC: Paul and I had a pretty good chat about where we stood with regard to where our dollars were. American Funds and Vanguard have gotten so specific. They had micro-funds and small funds and mid funds and large funds and giant funds. You can – We were kind of getting wrapped up. But you can – You need to have pieces a certain amount of pieces everywhere in order to maximize it and if the world's theory really was that small drive to the world, that they have the biggest part of any recovery, then small is where we have to be and have some of our money. We were talking about that last week. We do have quite a bit of debate on a regular basis, even before these meetings, talking about where we ought to be. And we're trying to manage thirty years from now. Not today, not next week, not whatever – but in the big scheme of things, where would positive investments be? Not giving up this year's return, but maximizing this year's return and next year, four years, five years, ten years. So that you have, you've built the whole thing.

??: One of the things I'll throw out and I don't know if you're interested in looking at this, but Goldman(?) Sacks(?) has a software package called a morning star x-ray, if you've ever heard of this and what you do is you load your investments into it, and it looks at the portfolio at a given point in time based on published holdings. They will tell you your overlap in all of the different funds, stock by stock and how much overlap you've got, and it will tell you percentages of where you are in all that style boxes of the morning style drift.

JC: That would be fun.

??: I think with the information I got here, I could probably throw that in there, but that would show you where you're concentrated.

JC: That would be good. I'd be interested.

PL: Do you have the Morning Star Report or golden stock?

??: It is a Goldman Sacks(?) piece of software that relies on morning style information, but it actually looks at the entire portfolio of what the mutual fund has got inside of it. What it will say is it will say —. Hey, if you've got Phillip Morris for example, which every mutual fund just about has in there any more, it will say, "You've got Phillip Morris in 6 of your 8 mutual funds, and the concentration is 15%." So if you think you've got diversification, you really don't. It will spell that right out.

JG: How quickly is that updated? Is that daily, or every six months?

??: It's updated as, I believe it's updated as often as the semi-annual and annual reports come out for the mutual funds. Because that's the only time we're going to get update information on the portfolios.

JC: The only time they really stop.

??: But it's similar to what Paul does on a simplistic nature, where he points out where we are with location management style, and so forth. It's similar to that. But what it does is it takes it to the next step. It grabs the individual securities within the fund and resorts that way, which makes it even more interesting as Mark pointed out.

JC: Right. Because we were working with a style boxes and working with macros and small purses. We had a couple that were misclassified. They were small purses instead of mini, or whatever the hell it was.   So we were having a discussion even last week about where we stand and whether we were prepared to do this and make a recommendation, or were we prepared to wait. We thought, "Well, we'll put it out here, because we've got this week's meeting, versus waiting until May." Then, things kind of went to pot again, so waiting doesn't seem all that serious. Cash is not a bad place to be. But I am interested in overlap. It would be kind of fun to see that.

MW: I'll send it to you.

JC: Of course, we could always make Smith Hayes do that for us.

PL: *(At the same time as MW)* Well, they have a formula.

MW: *(At the same time as PL)* If they can.

PL: I mean they have done that with the morning star report. I don't remember specifically that it puts something in style boxes, but they have done something similar to that.

JC: We had them do some of that, but it was a little bit wider. Not as specific.

PL: But it would be, if we get together in May, I'm just — I agree. I don't want to miss that $5 million for that pop.

JG: That's just — you know when I'm sitting here thinking, "I really —" Certainly you guys know way more about this than I do.

JC: But you do have cash. It isn't like we don't have and we're not making movements. Our job isn't to be market timers. I mean, that's really not our job. But we are investing for a long period of time.

PL: Well, we can accelerate this process, so you know if we — the longer we wait, if there is an upward movement, if we wait until June and we could have got in in April, then maybe we missed out on a couple of percent.

JC: Well, something's going to happen after the war starts, which is most likely going to be March or early April. People either are going to really think it was horrible or they're going to say, "You know, this wasn't as bad as we predicted."

PL: How about if I contact Smith Hayes and ask them to put something together at your earliest convenience and then we'll call another meeting if you guys have time to listen to what they have to say and what Mark has got too.

JC: Or maybe we could do a conference call, and talk about just the investment part. Say this is what we did.

??: Yes, depending on the temperature, I think that would be a good idea.

JC: Yes. It might be easier, because Aaron might be in the station. We might be able to pick him up versus I don't know a run or something. So we might be able to do a conference call as information. Because we are talking about buying things that already exist in parts of our portfolio anyway. Moving forward with money that we already have.

JG: Or we could just hold it a day. I mean, conference calls are okay, but it's not the same to me as sitting around the table.

JC: It isn't quite the same, but we are talking about a very limited issue. Not a global .... You know what I mean.

PL: Well, we'll see if we can arrange something.

JC: Yes, we've got time. You know it's not a complete agenda, Jim, is what I was talking about.

JG: You're right. No, no.

JC: If you're talking about a limited issue of what this is what we found and here's the documents, we mail it out, you got it a couple of days, and maybe we can get something accomplished.

PL: And speaking of accomplished. As I was talking to Mr. Donnelly, he made an excellent point. That was that the investment policy should be changed so that it specifies more clearly that it's okay for us to invest in Calvert's Income Fund. The policy gives us authority, although it could be seen as questionable, in that it allows investment in corporate bonds if there is investment in grade or better —.

[END OF TAPE 1, SIDE A]

PL: It has, what, you say 39% of the bonds are actually below investment grade. So —

??: Well, if you literally tear into our — which I'm sorry I did — permissible investments, there's nothing that mentions we can buy managed bond funds. So I made a recommendation to Paul and it's a pretty simple one that we add it so that we're covered.

PL: And the underlined — There's one underlined thing in here that doesn't cover it, but on page 2 of 6, it says, "permissible investments", I just added "managed bond funds" "can be purchased through professional money managers, mutual funds or brokerage accounts. The managed bond funds held by the plan must be traded on U.S. Exchanges." Because we don't want any Caymen Island funds. I just copied that language from right below it, 3A, Long Term Equity Investment, and stuck in "Managed Bond Funds" instead. So are there any — Because there's a couple areas that are also changed, but are there any edits to that?

??: No.

PL: To those two sentences? Okay. Then the next page, the next part down is credit criteria and quality rating. I added number 3, where it says, "Managed bond funds must have an average credit rating of investment grade."

??: Which in this situation is A or better.

PL: Okay. That depends which — Um, doesn't it depend which credit rating agency?

??: Yes. Which is not covered in here.

PL: Yes. I mean that's why I just said "investment grade", because I think one of them is "EAAA", and another one is some other letter. *(Indecipherable)*

??: If I remember right, Morning Star goes with one and Libber goes with the other, so.

JC: That's right.

PL: Well, I mean, if we, if you know them both, I can put them both in here. Otherwise we can leave it as "investment grade." Either way is fine with me.

??: No, that's fine.

??: I don't think you want to be too close. Quite honestly. I mean I think you want to — I think you want to leave yourself wide open to whatever investment grade, because it could differ.

PL: Then on page 3, for maturity guidelines, I inserted the word "individual", because Mr. Donnelly pointed out that with a managed bond fund you never know what the exact maturity rate of that is. So I changed it to say "individual corporates", which we have no plans in purchasing, but they shall, if we would, they'd be the maximum maturity of ten years. That's just something that would go in and have. And then, on page 4, I put a number in here, but it's up for editing. Portfolio structure, E5, the managed bond funds must be less than 20% of the plan's assets.

??: Why don't we move 5 up to one and say, "Debt securities, including managed bond funds, must be at least 50% of the plan assets"?

PL: Okay. Is that okay with everybody?

??: That way we're not really creating another category there.
??: That's fine.

PL: All right. Then this last underline on that page is an old one that we passed a long time ago?

??: Do we want number 1 to say, "must be"? Or "should be"?

PL: Well, we've always — We've had it at "must", because —

JC: "Must" is still not absolute. I mean "shall" is mandatory. I mean, if you really wanted to — If you really wanted it to be an absolute, it has to, it should be "shall be". "May be" is extremely flexible and "must" is gravy. So how — It doesn't matter to us. But in terms of terms of art, you know.

PL: Well, if we say "should", that's a little too vague, we were originally thinking.

JC: But since it is a —

??: But again I'm just thinking in the next few years when get growth potential back on the market, then all of a sudden we have an allocation that's 60-40, we'd have to sell?

??: Oh, yes.

JG: So we'd be forced to sell?

JC: Well, you're going to — and Paul and I have been talking about periods of points of rebalancing no matter what anyway. You know selling to rebalance. I think it's something we'll have to visit anyway. As a part of looking at a strategy for long term rebalancing. So whether we change it today or we look at it as a Committee to say if our portfolio theory is 60-40 or 40-60, whatever it is, at what point do we rebalance? Do we do it annually, quarterly? You know, we need to get a theory where we balance to whatever structure, if that's —

??: That's why I was bringing up if the work changed, just in case anybody ever challenges us, we can say, "Look at the number of months that you were over 50%. You know you were under 50% on your bond, and it says clearly in your document that you "must be".

JC: Right. I think it merits some continued discussion, because I think we do need a definitive discussion with regard to rebalancing, and revisiting what our long term portfolio goal ought to be. What we've been talking about is the efficient frontier and what part of that was in your material, what our asset allocation ought to be long term. Then where we plug in rebalancing to buy and sell. So —

??: Just so it comes up on the agenda. You know, in three months, six months, nine months, from now, that's fine.

JC: I think it ought to be back in — We've been looking for you guys to, with regard to guidance, so if you think re-balancing annually is something that — or semi-annually, however you see it. Since we are long term issue, then if we go over and we put re-balancing in here, if you're plus or minus two or three percent, we're not selling that week to re-balance. We are looking at the end of a year, or looking at an optimum time to re-balance. So if you guys want to jot some notes so when we meet in the summer or something about that issue, I think that's a relevant topic we ought to be visiting.

??: Okay.

PL: And that's all for changes.

??: Move we accept.

??: Second.

JG: All in favor?

(Present committee members say, "Aye")

JG: Okay.

PL: A review of recent events and our one new action. Are there any other ....?

??: Do we need to table that action?

PL: Oh. Actually I was thinking the action would be the change to the investment policy.

??: Okay. Do we need to table your recommendations?

PL: That's fine.

JC: It's up to you, if you want to take a vote on it. Tabling it. That's fine with us.

??: I think we probably should as a committee.

??: Make it official. Yes.

??: I'll move that we table the asset investment plan recommendations as presented.

JG: Is there a second?

??: Second.

JG: All in favor?

(Present committee members say, "Aye")

JG: Opposed?

(Silence)

JC: If it's acceptable to everybody, let's put for the August meeting the discussion with regard to balancing, or re-balancing.

??: That sounds good.

JC: I mean I think May is going to busy with regard to other discussions it looks like. Funding not being the shortest of those. So let's put it on August, the discussion of re-balancing. Gives us plenty of time to talk about that. And then we'll have some asset reallocation discussion, in May as well.

PL: That's all we have. Any new business?

JG: I just had one thing I wanted to ask you about. That was the additional investment for DROP. Did you hear any more about that?

PL: No. I haven't done a darn thing since I talked to you. I've been working with the computer person, explaining stuff to her, *(indecipherable)* stock.

JC: We are going to ask for legal guidance. With regard to that, and with other issues.

JG: *(Indecipherable)* conversation I —

JC: And that still needs to go forward. But that is not — we're not dropping that, so.

JG: Okay.

PL: I think in the back of my mind it isn't the highest priority that I have, because I figure that that probably won't happen until .... Well, we actually, we don't need the Mayor's or the Council's approval on that.

JC: No. No, we just need some legal guidelines actually, Jim. I read in the, unfortunately some of the things come to us officially, and some you read in the paper, and some you don't, but the Bush administration has proposed last Friday pretty sweeping changes to 401K's, 403B's, 457's, in total allowable contributions, that might dramatically change what we would be allowed to do. And I would have said it doesn't have a snowball's chance in hell of passing, but both the House and the Senate and the President are all Republicans. So it has a better chance of passing today then it might have two years ago. I mean there will be arguments over it, but the votes would probably be there to pass some change. Maybe not the way they proposed it. So, your increased limitation, we might be able to get a definitive answer on that, and what you could do in conjunction with two or three other investments, but if they pass that relatively quickly as they may, then we may be looking at different parameters with regard to total contributions into funding sources. What I took off the internet was that there were three new styles. The IRA would disappear.

JG: Sounds pretty drastic.

JC: Yes. The 401K and 457 would become an employer sponsored retirement account. Then there was something I didn't understand called the lifestyle account, which said tax deferred savings account you could use for anything, which didn't make any sense. But —

??: Like a Roth IRA.

JC: Yes. So there were, and I think it had $7500 limit but no income. Something like that. So there were three new plans and I don't know how that would impact additional contributions to anything else. It's not that we don't have an interest in that, but I thought we had a fairly good handle on what we were going to ask for a total. Paul and I and Georgia talked about what we were going to ask Icemiller(?) with regard to what the total amount of contributions you could make or a person on the DROP could make, voluntary, both to that and to deferred comp and whatever else you were going to do, and what the maximum amount was, and get their opinion. So we're comfortable that their pension is correct, and then I saw this material. But it doesn't mean we're not moving forward. I just wanted you to know that they're proposing at least some changes that might be relatively sweeping to what we're asking.

JG: Okay. I guess from a personal standpoint, I would hope that you move forward with it, because I am personally prepared to utilize that in my DROP account.

JC: Right. Now, and then, you have a year from October, you know, you can double up on your 457, if it still exists.

JG: Yes. I've done that already. That's —

JC: No. You can add another $15,000.
JG: Oh, yes. Um hm.

JC: A year from October. So, all is not lost, but we need to get an answer with regard to your total contributions. Or anybody's total contributions, I should say.

JG: Didn't you get one? A $40,000.

JC: Well, we have a general answer with regard to a bulletin that they put out, but we're talking about whose responsibility it is to monitor those contributions. Is it ours as a plan to monitor your contributions to us, at the same time you do a four oh — and we don't know if that includes a SEP or any of the other contributions. So we have some minor questions to ask. It's not as big a deal, and as soon as we get over some rough spots, we'll ask the questions. But I think we'll get that resolved before we meet again. Or at least get the question answered.

PL: Yes. I'm — After this meeting, well, let's say I have to calculate the pension earnings rate for January. That might take Friday, but then next week I would think that I have time to write a letter advising *(indecipherable)*.

JC: That request is pretty straightforward.

JG: That's what I was thinking. Okay, thank you.

JC: Some aren't. But that one is.

JG: Appreciate that. Okay. *(Pause)* Okay. That's it?

??: That's it.

JG: Then you guys can adjourn.

[END OF MEETING - SOUND OF TAPE BEING TURNED OFF]